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TAGS: ETRD ECON EAGR AR BR
SUBJECT: Argentina: Global Crisis Threatens Export Growth, Trade Surplus

Reftels: A. Buenos Aires 1389
¶B. Buenos Aires 1374
¶C. Buenos Aires 1415

Summary

¶1. (SBU) Argentina's strong goods export performance in the aftermath of the 2001/02 financial crisis has stalled, a victim of plunging world commodity prices and slower global growth projections. From a projected 2008 trade surplus in the $12 billion range, local economists now see the 2009 surplus dropping to under $6 billion - and that assumes current commodity price levels are sustained. Maintaining a substantial trade surplus has been a pillar of the GoA's economic model because it has supported the accumulation of dollar reserves, suits the mercantilist and protectionist mindset of current decision-makers, and plays well domestically with the powerful and employment-generating industrial sector. A GoA concerned that key trading partners' substantial devaluations will harm Argentina's relative competitiveness (the Brazilian real has dropped 21% vis the peso since August 7) and sensitive to industrialists' calls to protect domestic production and employment has introduced a variety of non-tariff barriers and allowed a managed peso depreciation of over 10% vis the dollar over the past six weeks. Keeping exports up is also important to the GoA because a significant share of proprietary federal revenues cmes from export tariffs, especially on agricultural commodities. Agricultural and industrial exports, and the tax revenues they generate, are front and center in the GoA policy response to the financial crisis. End Summary.

Argentina a Beneficiary of Soaring Commodity Prices

¶2. (SBU) Between 2002 and 2007, the value of total annual Argentine goods exports more than doubled from US$26 billion to $56 billion. During this same period, agricultural exports were the star performer, jumping 140% from $12 billion to $28 billion, and rising from 46% to 51% of total exports. As a consequence, Argentina maintained a healthy overall trade surplus, reaching $11.1 billion in 2007, after a record of $12.4 billion in 2006.

¶3. (SBU) Argentina's global exports in 2007 totaled $55.9 billion, a 20% increase y-o-y. According to official GoA statistics agency INDEC, this jump was driven by a 12% increase in the price of exported goods and an 8% rise in quantity of goods exported. 22% of 2007 exports by value were "primary products" led by cereals, oilseeds, copper, fresh fruit and fish, which saw a 23% price increase, as well as an 18% quantity increase. Processed agricultural goods, at 35% the largest category of Argentine exports, saw a 22% price increase but only a 3% increase in quantity.

¶4. (SBU) The y-o-y price increase trend was even more pronounced during the first eight months of 2008. Within overall export increases of 34% in price and 4% in quantity (and 39% in total

value), primary product prices rose 49% while quantities increased only 4%, accounting for a 55% total increase in value. The value of processed agricultural goods exports rose 40%, thanks to a 49% price increase, which more than offset a 6% quantity decrease (presumably at least partly caused by the extended agricultural strike).

Global Weakening and Commodity Price Plunge Bites
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¶5. (SBU) In recent months, due in large part to the dramatic slowdown in global growth forecasts, global commodity prices for Argentina's primary exports have fallen precipitously. The Argentine Central Bank (BCRA) tracks a commodity price index which includes soy, wheat, corn, petroleum, steel, aluminum, beef and copper, weighted by share of total Argentine exports. Together, these commodities represent 40.5% of 2007 Argentine exports. After peaking in June, up 67% y-o-y in dollar terms, the index fell over 18% by end-September, though the index remained 18% higher than in September 2007. Prices for soy, Argentina's top export and emblem of Argentina's efficient agricultural growth, dropped 39% from a July 2008 high of $588 per metric ton to $360 as of October 29.

¶6. (SBU) As a consequence, private analysts are reducing their projections of Argentina's trade surplus in 2009. According to the 2009 budget presented by the GoA to the Argentine Congress September 15 (Ref A), total 2008 exports were estimated at $73.5 billion, a 32% increase over 2007, with a trade surplus of $12.2 billion. 2009 budget exports were projected to be $78.3 billion, and the surplus $12.0 billion. Some private estimates are less optimistic. For example, internationally known Argentine economist Miguel Angel Broda has sharply reduced his export performance estimates for 2009. Broda's "optimistic" estimate for 2009 shows exports of $73.4 billion and a trade surplus of only $5.9 billion, roughly half the

GoA's estimate. Broda's "pessimistic" outlook foresees exports of $65.2 billion - and a net trade deficit of $1.2 billion, which would be Argentina's first trade deficit since 2001. HSBC's Chief Economist predicts the 2009 trade surplus will be in the range of $5-6 billion, less than half his estimate from earlier this year.

¶7. (SBU) Credit Suisse, which as recently as September estimated that the 2008 current account surplus would be $5.2 billion (after $7.3 billion in 2007) and 2009 surplus at $2.6 billion, downgraded the latter estimate to $1.5 billion. The global crisis was the driver behind this downgrade, as the bank cited both lower commodity prices and lower foreign demand for non-commodities as reasons that Argentina would have "nearly zero growth in the dollar value of total exports." Local think-tank FIEL is even more pessimistic, projecting a 2009 current account surplus of just $800 million in
¶2009.

Non-Transparent Budget Trade Surplus Estimates
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¶8. (SBU) Commodity price assumptions are not explicitly stated in GoA budgets. However, local business daily Ambito Financiero quotes a Ministry of Economy official involved in the budget's formulation as saying the assumed price for raw soybeans would average $420 per ton in 2009. As of October 22, the price of soybeans stood at $340/ton - 19% lower. In 2007, Argentina exported 26 million tons of raw soybeans. The $80 price drop, with the same quantity of exports (though soy exports are predicted to be higher in 2009 than in 2007), translates into a drop of $2.1 billion in export value. The 19% drop, if applied to all commodities in the BCRA index, would result in a loss of $5.6 billion of exports - the equivalent of 47% of the trade surplus estimated in the official GoA budget.

¶9. (SBU) According to Embassy Economy Ministry contacts, budget estimates are made at a fairly high level of government, without technocrat-level consultations. Adrian Makuc, National Director of Trade Policy in the Ministry of Economy, told Econoff October 16 that, while his office used to have input into the trade numbers used in the budget, "Now I read about them in the paper, just like you." When asked about the possibility of the GoA presenting a revised budget to Congress, rather than continuing to seek approval of the one already presented, he added, "There seems to be more concern (within the GoA) about getting the budget passed than correcting the numbers."

Impact of Peso Depreciation on 2009 Trade Balance
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¶10. (SBU) According to INDEC, industrial products represented 31% of export value in 2007 - roughly half of the 57% of export value contributed by primary commodities (excluding hydrocarbons and precious metals) and processed agricultural goods. With the run-up in global commodity prices, in the first eight months of 2008, industrial products' share of the value of exports fell to 29%, while commodities and processed agricultural goods rose to 60%. Concerns over the increasing relative strength of the Argentine peso against major trading partner currencies, most notably Brazil's real (Ref B) - have ed to calls by manufacturers for an immediate and substantial peso devaluation to maintain competitiveness. The Central Bank has managed an over 10% devaluation of the peso over the past six weeks from 3.05 to 3.38 (as of October 27). Local analysts agree that, all other things equal, a devalued peso should stimulate additional primary commodity export production and so support Argentina's trade balance on the margin.

Note: The budget assumed an average 2008 exchange rate of 3.19 pesos per dollar (through October 16, the ytd average was 3.11 according to the BCRA), and 3.34 in 2009. With Cabinet Chief Sergio Massa announcing expectations of the exchange reaching 3.35 by the end of 2008, and presumably even lower in 2009, it appears to be an admission by the GoA that the exchange rate and projected trade surplus included in the 2009 budget cannot both be achieved. End note.

Comment

¶11. (SBU) Maintaining a large trade surplus has been a pillar of the GoA's economic "model", partly because it suits the mercantilist and protectionist mindset of its current decision-makers, but also because it plays well domestically to big industry, a traditional foundation of Peronist support in Argentina. A GoA concerned that trading partners' substantial devaluations imperil its relative competitiveness (Brazil's real has fallen 21% vis the peso since August 7) and sensitive to industrialists' calls to protect domestic production and employment has introduced a variety of protectionist non-tariff barriers (Ref C) and has allowed a managed peso depreciation of over 10% vis the dollar over the past six weeks. Countervailing arguments that a peso devaluation is potentially

inflationary have been discounted in light of a dramatic drop in domestic growth projections: 2009 GDP forecasts have been progressively lowered from 6-7% just six months ago to the 1-2% range today, with some economists now projecting recession. Keeping exports up is also important to the GoA because a significant share of proprietary federal revenues not automatically shared with provinces comes from export taxes, especially on agricultural commodities. Trade flows - agricultural and industrial - and the tax revenues those export flows create, are front and center in the GoA trade policy response to the financial crisis.

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